

Arizona Intends to Clarify Taxation Of Digital Goods and Services

by James G. Busby Jr.

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In this edition of SALT From My Saddle, Busby says that Arizona's effort to clarify the application of the state's sales tax to digital goods and services is gaining momentum and offers predictions about significant provisions that may be in anticipated legislation.

The author helped draft this proposed legislation.

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The Arizona Joint Legislative Ad Hoc Study Committee on the Taxation of Digital Goods and Services¹ completed its work and issued its recommendations in December.²

¹ See Busby, "Arizona Is Reexamining the Taxation of Digital Goods and Services," *State Tax Notes*, Sept. 4, 2017, p. 967, for more information about the reason for the committee and its charge.

² See Arizona State Legislature news release, "Business Community Rallies Around Legislative Recommendations of Ad Hoc Committee on Digital Goods and Services" (Dec. 22, 2017) for details concerning the committee's recommendations.

Legislation Expected

With broad support from the state's business community, key lawmakers introduced legislation to clarify the application of Arizona's sales tax to digital goods and services in January.

House Ways and Means Committee Chair Michelle Ugenti-Rita (R) and Senate Finance Committee Chair David Farnsworth (R) co-chaired the committee and dropped companion bills in their respective chambers that would update Arizona's tax statutes to address and stimulate this burgeoning area of our economy.³

Ugenti-Rita stressed the need for clarity and the importance of alleviating administrative burdens to "foster continued growth in Arizona's technology economy."⁴ Arguing that Arizona's tax statutes "have not kept pace" with our digital economy, Farnsworth emphasized that "we need to ensure that Arizona has a modern tax environment that is predictable, transparent and fair for all taxpayers."⁵

Senate President Steve Yarbrough (R) indicated his commitment to working with the governor, the House, and fellow senators on the issue.⁶ And business-friendly Gov. Doug Ducey (R) — like he has in similar situations in the past — is expected to champion the legislation, which would promote the growth of the digital economy.⁷

³ See H.B. 2479 and S.B. 1392.

⁴ *Id.*

⁵ *Id.*

⁶ *Id.*

⁷ E.g., in 2015 and 2016 Ducey signed tax legislation to promote the sharing economy in Arizona, and when California regulators shut down Uber Technologies Inc.'s self-driving cars, Ducey welcomed them to the state, saying, "California may not want you, but we do." Busby, "Arizona Tax Changes to Welcome the Sharing Economy," *State Tax Notes*, Feb. 6, 2017, p. 517.

Insider Predictions

While Arizona's legislative session began January 8, the bills that Ugenti-Rita and Farnsworth introduced have not been heard in committees yet, and the final legislation — if any — may be different from what was introduced. As drafted, the bills would:

- define “prewritten computer software” and permit the Department of Revenue and cities to impose retail sales taxes on proceeds from prewritten computer software regardless of delivery method;
- define and prohibit the DOR and cities from taxing proceeds from specified digital services, including software as a service, platform as a service, infrastructure as a service, application service providers, hosting services, data storage management, data processing and information services, streaming services, digital authentication services, and any other cloud-based or other remotely accessed computing services;
- define specified digital goods to include digital audiovisual works, digital audio works, and digital books;
- permit the DOR and cities to tax proceeds from sales of specified digital goods as retail sales if transferred in whole to a customer rather than merely streamed over the internet;
- prohibit the DOR and cities from taxing proceeds from specified digital goods streamed over the internet rather than transferred in whole to a customer; and
- outline sourcing requirements and permit vendors to accept a multiple point of use certificate that the DOR will create.

Stay tuned, because along with how the Legislature responds to the projected increase in state income tax revenue from the federal Tax Cuts and Jobs Act of 2017, this is likely to be the biggest tax issue it addresses this year. ■

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